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Federal Communications Commission
Office of Secretary

**Ex Parte**

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W. Rm. 222
Washington, D.C. 20554

**Re: CC Docket Nos. 96-262 and 96-45**

Yesterday, Ray Smith, Jim Cullen, and the undersigned representing Bell Atlantic met with Chairman Reed Hundt, Regina Keeney - Chief of the Common Carrier Bureau, and Tom Boasberg - Legal Advisor to Chairman Hundt, to discuss the above referenced proceedings. The attached material was used during the meeting. Due to the late hour at which the meeting concluded this ex parte is being filed today.

Please enter this letter and attached material into the record as appropriate.

Sincerely,

Ed Young

Attachment

cc: Hon. R. Hundt
R. Keeney
T. Boasberg

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<u>Access Reform/Universal Service Talking Points</u>

April 24, 1997

- Based on recent conversations with FCC staff, it appears that the Commission is likely to adopt orders in the access reform and universal service proceedings that would:
  - Maintain existing levels of universal service support for rural America
  - Fully fund schools and libraries
  - Implement a more economically efficient access rate structure that lowers usage charges and recovers non-traffic sensitive costs on a flat rate basis.

<u>Bell Atlantic supports these objectives and would support them publicly.</u>

- We have two major concerns, however, with regard to the direction the Commission may be headed: (1) the adverse effects of a possible increase in the price cap productivity and (2) the level of the per-line charge on multiline businesses.
- Our first concern is that the staff is considering a proposal to raise the productivity factor. **Any significant increase in the current 5.3% productivity factor is not justified and not necessary.**
- Long distance carriers do not need to increase toll rates if the productivity factor remains at 5.3%.

-- **With the current 5.3% offset, the Commission could fully fund education and other universal service obligations without triggering the need for any toll rate increase by the long distance carriers.** As the attached chart 1 shows, while interexchange carriers might have a brief period of deficit, they quickly move to a point where they are significantly better off than they are today.

-- Moreover, the chart understates the positive impact to long distance carriers in two ways. First, it assumes that all universal service funds for schools and libraries will be paid up front. In fact, if they are paid at the rate of actual usage, the deficit for the long distance carriers would be much smaller and would turn around to a positive for them in a shorter period of time. Second, the long distance carriers will also benefit from increased demand for long distance service due to lower per-minute rates beginning January, 1998.

- Even though access charges have declined as a percentage of long distance revenues (Chart 2), these reductions have not been fully reflected in their toll rates.

- The current record does not justify a higher productivity factor:

  -- Economic data (Total Factor Productivity studies) support a productivity offset that is significantly below the current 5.3%. Even an update based on the methodology the Commission has previously used does not support an increase in the productivity factor.

  -- Even with a 5.3% rate reduction, Bell Atlantic's current earnings would fall below 10.25%, the level at which LECs may today be considered under-earning and allowed to increase rates.

  -- A significant increase in the X factor would only exacerbate the problem and would serve to penalize lower earning LECs. As shown in chart 3, if, as some staff members have suggested, the productivity factor were increased to 6.5% and rates were reduced as if that level had been in place last year as well as this year, Bell Atlantic's current rate of return would fall all the way to 9%.

  -- Claims that Bell Atlantic has lower earnings because it it an inefficient carrier are just plain wrong.

  Bell Atlantic has the lowest access rate in the nation (2.1 cents per minute of use), and has been one of the lowest cost carriers since divestiture. We are also among the carriers with the lowest number of employees per access line.

  Moreover the lower interstate returns Bell Atlantic passed this year reflects the previous disproportionate price cap rate reduction ($294M) the company took in 1995. If Bell Atlantic's rate reduction had been similar to Ameritech's ($65M), our earnings this year would have been significantly higher.

- Our other major concern is that the staff's recommendation would result in unduly high per-line charges for multiline businesses.

  -- This puts LECs at a disadvantage in competing for the business of our most competitive market segment, and increases the likelihood that LECs will not be able fully to recover these charges from business customers.

  -- In addition, the higher charges exacerbate an existing competitive disadvantage with respect to unbundle lines. The Commission requres that unbundled elements be priced on a geographically deaveraged basis. In contrast, SLC and PSL charges are priced on a state-wide basis. Therefore, in low cost areas, unbundled elements already are price d lower. Placing additional costs on SLCs on PSL charges only serve to increase that differential.

-- That high differential in turn will give these customers an incentive to not presubscribe their lines or to avoid the charges by moving to a carrier that offers them service using our unbundled facilities. Because unbundled network elements carry no SLC or presubscribed line charge, loss of these customers will result in a greater cost recovery burden on our remaining customers.

-- This also places a much higher burden on our Centrex customers than it does on PBX customers with equivalent service. For example, even a medium-sized Centrex customer with 100 lines would pay $74 a month in additional SLC and would have a PSL charge on their lines of $450 a month (total $524). In contrast, an equivalent PBX customer would only pay $7.40 in additional SLC, and have a $45 PSL assessment (total $52.40) -- a tenfold difference.

-- As shown in chart 4, these competitive concerns could be ameliorated without a significant increase in the per minute rate if :

- the multiline business presubscribed line charge were capped at $2.00 rather than $4.50;

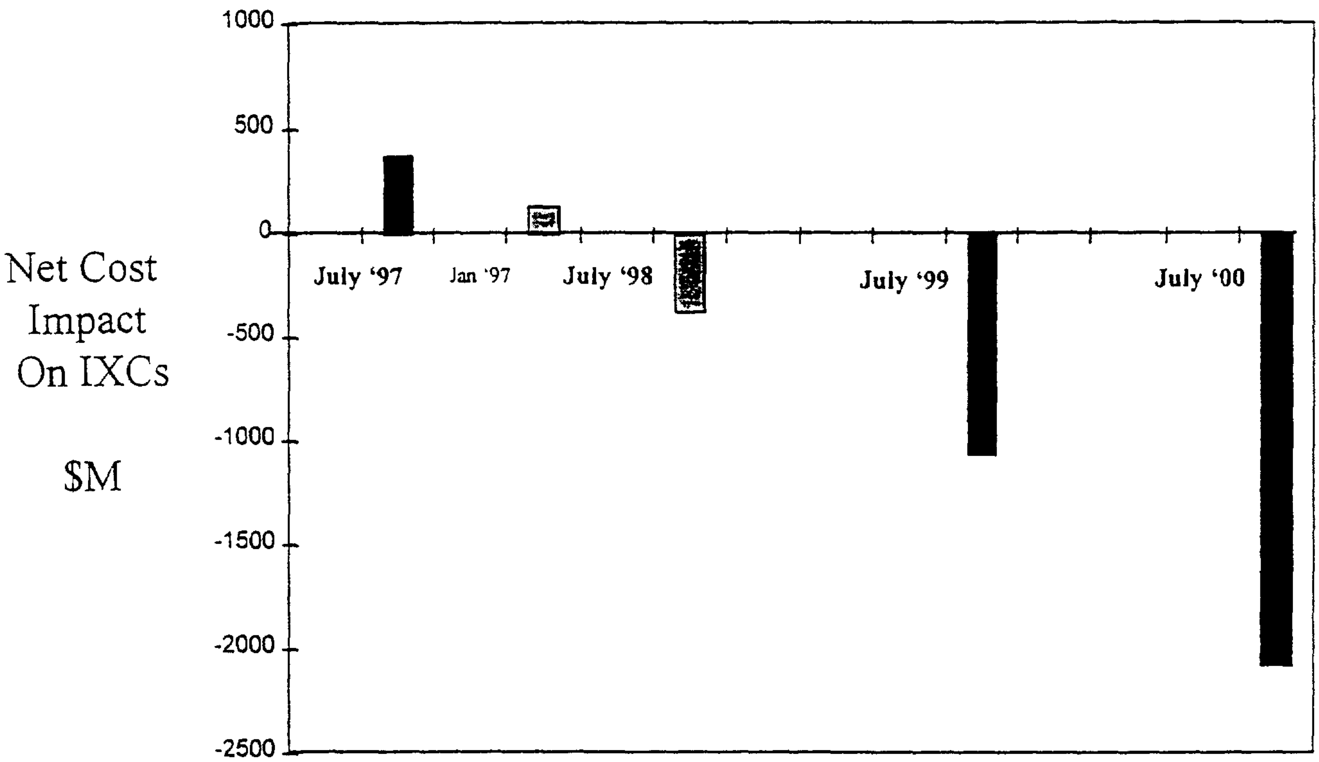
- the residential presubscribed line charge were capped at $1.00 rather than 75 cents;

- the second residential presubscribed line charge were maintained at the $1.50 recommended by the staff; and

- the overflow in excess of the presubscribed line charge went equally to originating and terminating usage rates.

-- This approach would avoid radical changes in the presubscribed line charge and accompanying rate shock to multiline business customers. It would nevertheless bring originating and terminating usage rate to the same level as the staff has recommened by 1999.

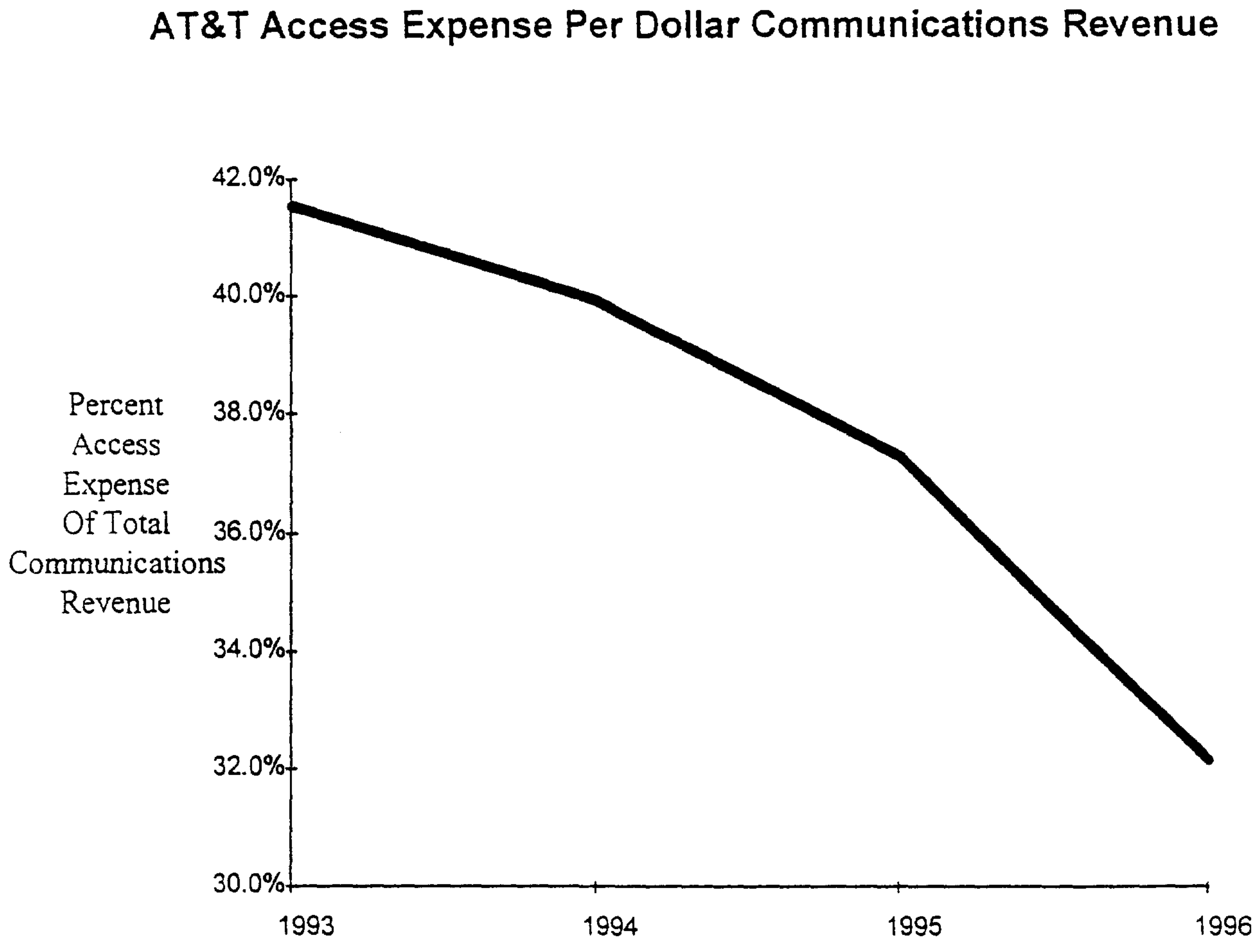
# Long Distance Carriers Benefit At 5.3% Productivity Offset




* - Excludes benefits from demand stimulation

With the current 5.3% offset, the Commission could fully fund universal service obligations without triggering the need for any toll rate increases by the long distance carriers

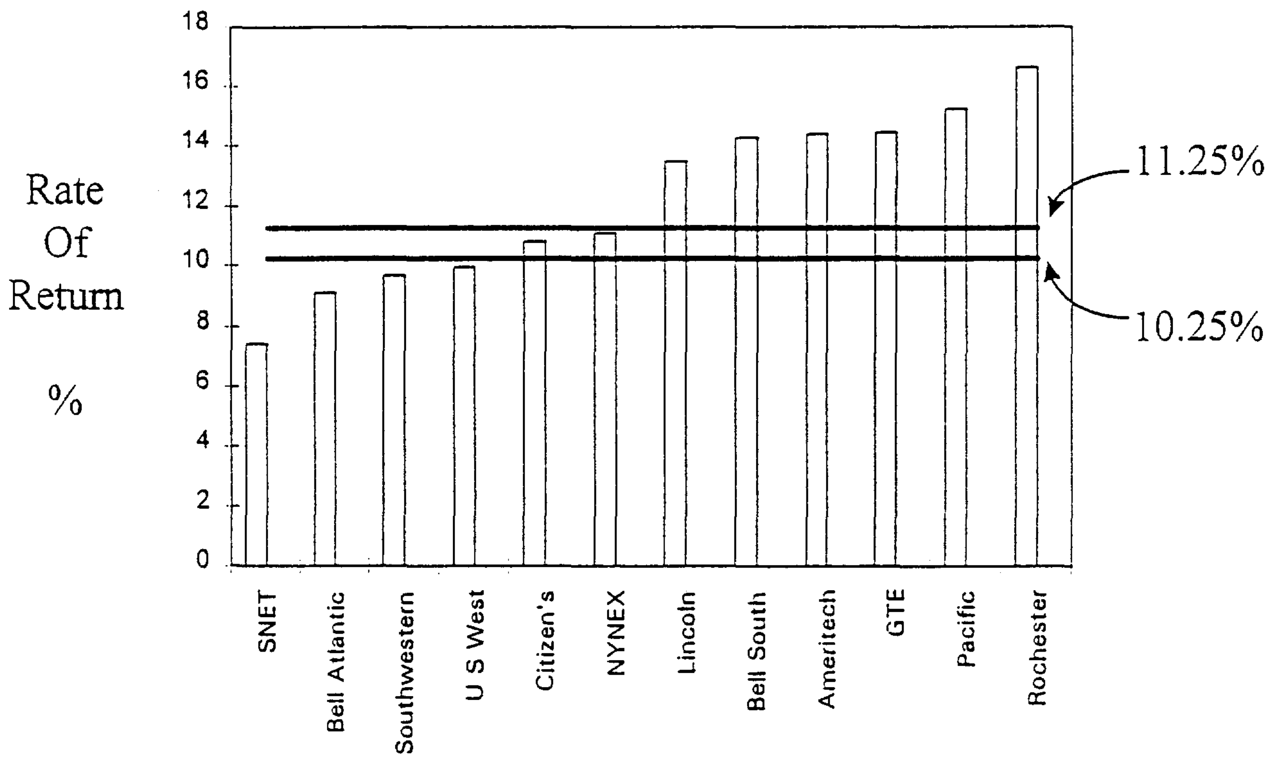
# Access Charges Have Fallen Relative To Long Distance Revenues




Source: AT&& 1995 Annual Report and AT&T 1996 Investor Relations Quarterly Bulletins. Communications revenue includes wireless and wireline revenues. Access includes other interconnection expenses.

# Price Cap Adjustments Should Be Subject To An Earnings Floor

Annual Filing With 6.5%/7.8% Adjustment for 96 and 97

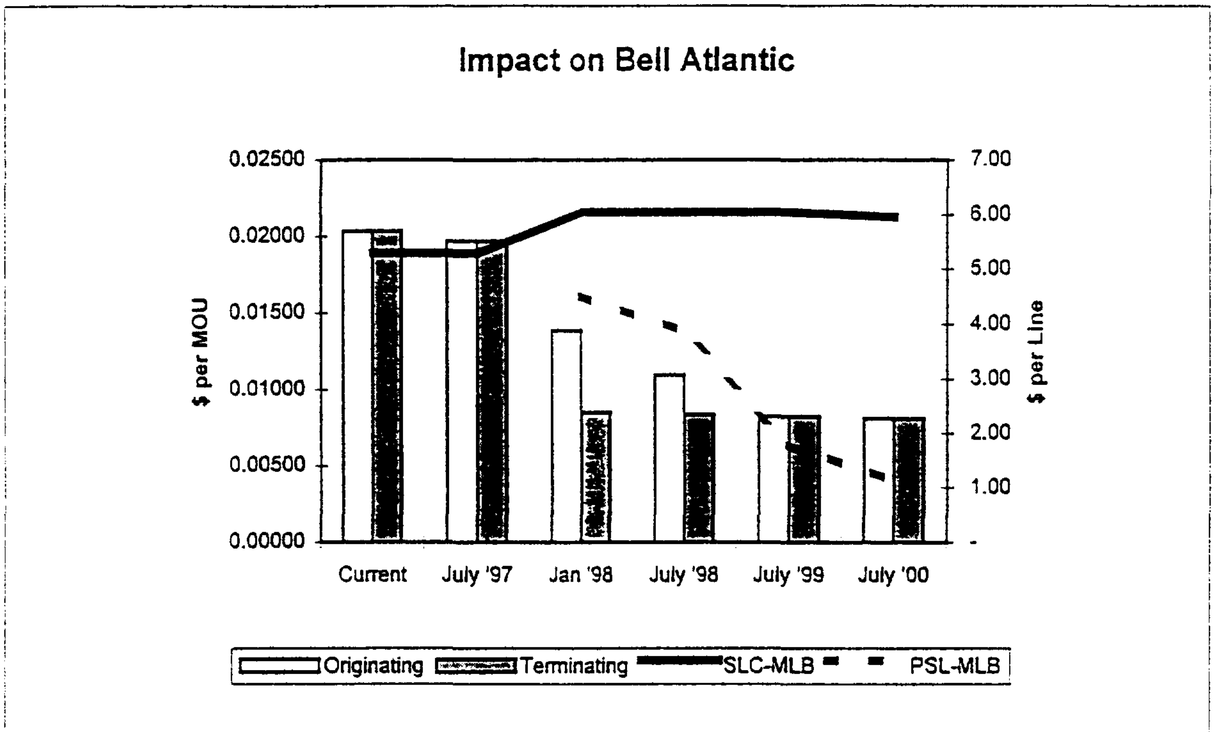



Sound public policy would not push earnings below a level the Commission has already determined to be a floor (10.25%). If the price cap is lowered as if an increase in the productivity factor had been in effect in both 1996 and 1997, in no event should any adjustment take a company's earnings below the 10.25% earnings floor.

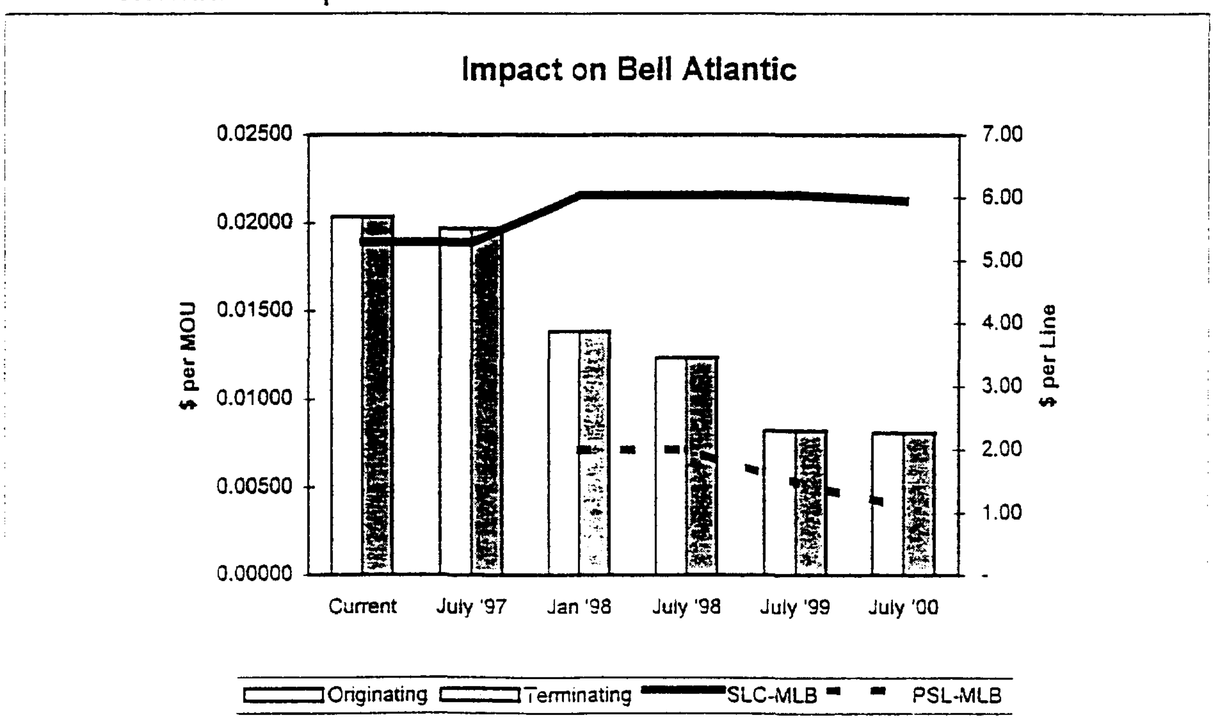
Chart 4

## The FCC can achieve the same long-term rate reduction objectives and avoid short-term rate shock on business customers

FCC Proposal:




Alternative Proposal *:




* Assumes a $1.00 Res PSL, $1.50 2nd Line PSL and a $2.00 MLB PSL
Also assumes reductions are equally applied to both originating and terminating rates